**Frank S. Simone**
Government Affairs Director

Suite 1000
1120 20th Street, NW
Washington DC 20036
202-457-2321
202-263-2660 FAX
fsimone@att.com

October 31, 2003

VIA ELECTRONIC FILING

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
445 Twelfth Street, S. W. – Room TWB-204
Washington, D. C. 20554

Re: *Ex parte,* CC Docket No. 96-149, Verizon Petition for Forbearance from the Prohibition of sharing Operating, Installation, and Maintenance Functions Under Section 53.203(a)(2) of the Commission's Rules

Dear Ms. Dortch:

Attached please find AT&T's response to Verizon's October 27, 2003 submission in the above-captioned proceeding.

Consistent with Section 1.1206 of the Commission's rules, I am filing one electronic copy of this notice and request that you place it in the record of the above-captioned proceeding.

Sincerely,

ATTACHMENT

cc: B. Tramont
C. Libertelli
M. Brill
J. Rosenworcel
D. Gonzalez
L. Zaina
W. Maher

AT&T

Aryeh S. Friedman
Senior Attorney

Room 3A231
900 Route 202/206 North
Bedminster, NJ 07921
Phone: 908 532-1831
Fax: 908 532-1281
EMail: friedman@att.com

October 31, 2003

VIA E-MAIL

Marlene Dortch
Secretary
Federal Communications Commission
445 12th Street, S.W., TW-A-325
Washington, DC 20554

Re: *Verizon Petition for Forbearance from the Prohibition of Sharing Operating, Installation, and Maintenance Functions Under Section 53.203(a)(2) of the Commission's Rules*, CC Docket No. 96-149

Dear Ms. Dortch:

AT&T Corp. ("AT&T") hereby responds to Verizon's October 27, 2003 *ex parte*.

***First, AT&T has made it clear that it seeks a "level playing field," not protectionism.*** AT&T has repeatedly invoked the "reality of the market" – that Verizon has been able to capture substantial interLATA market shares shortly after receiving section 271 authority even with the OI&M safeguard in place – to demonstrate that the OI&M has imposed no meaningful costs on Verizon. AT&T has not, as claimed by Verizon, made "a plea for protectionism."[1] To the contrary, as AT&T has demonstrated throughout this proceeding, the OI&M safeguard is necessary to ensure that the BOCs compete on a *level playing field*, placing BOCs and their affiliates in the same position as their competitors in the local and interLATA markets.[2] Moreover, the need for a level playing field is as necessary in the business market as in the residential market because Verizon and the other BOCs maintain a firm grip on critical inputs in the business market, such as special access.

---

1 Verizon's October 27, 2003 *ex parte* at 1.
2 Letter from David L. Lawson on behalf of AT&T to Marlene Dortch, Secretary, Federal Communications Commission, November 15, 2002, at 1.

***Second, Verizon's ex parte does not refute that it uses the "prevailing price" loophole to structure its affiliate transactions in a manner that is economically irrational except for the fact that it will benefit its section 272 affiliate (and perhaps tangentially other smaller unaffiliated entities). Nor does Verizon's ex parte refute AT&T's showing that post-conduct audits are no substitute for structural safeguards.*** As noted in AT&T's October 1, 2003 *ex parte*, Verizon has structured its affiliate transactions, such as its billing and collection service, so as not to offer discounts based on volume of business (which might be economically rational to the extent that the discount reflects volume-related savings that would be passed on to purchasers), but rather to offer discounts based upon a specified percentage of business (e.g. 85% of *total* Verizon end user billing).

Because a percentage of billing discount does not correlate with savings that might be realized by Verizon, Verizon's offer effectively limits the discount to Verizon's Section 272 affiliate and perhaps other smaller competitors. Such pricing arrangements have, in other contexts, been seen by the Commission precisely for what they are – attempts to discriminate in favor of the BOC's section 272 affiliate.[3]

Moreover, Verizon's claim that there is a biennial audit of the CAM,[4] in no way refutes AT&T's demonstration of the limited utility of post-misconduct audits, particularly in light of Verizon's demonstrated efforts to delay issuance of the audit data. Indeed, Verizon continues to delay the release of critical audit data. It has just recently petitioned for review of the Commission's order denying its request for confidentiality for the most recent Section 272 Biennial audit,[5] even though Verizon lost the very same motion with respect to its first Section 272 Biennial audit. As a result of Verizon's actions in the first Section 272 audit proceeding, Verizon was able to delay the release of the audit data for almost a year and a half after it was collected.[6] By doing it again with respect to the

---

3 *See Access Charge Reform*, Fifth Report And Order And Further Notice Of Proposed Rulemaking, 14 FCC Rcd. 14221 (1999) ¶ 134 (The Commission specifically noted that "growth discounts," which offer reduced prices based on growth in local traffic, "create an artificial advantage for BOC long distance affiliates with no subscribers, relative to existing IXCs and other new entrants"). *See also,* Comments of AT&T Corp., WC Docket No. 02-150, at 47-51 (filed July 11, 2002) ("AT&T Alabama 271 Comments") (BellSouth similarly proposed a tariff that would establish a discriminatory growth discount that would favor BellSouth's long distance affiliate over large, established IXCs such as AT&T).

4 Verizon's October 27, 2003 *ex parte* at 2-3.

5 *See* Verizon's Application for Review in EB-03-IH-0341 filed on August 14, 2003.

6 *In the Matter of Accounting Safeguards Under the Telecommunications Act of 1996: Section 272(d) Biennial Audit Procedures*, Memorandum Opinion and Order, CC Docket No. 96-150 (rel. Jan. 10, 2002). Verizon filed a Petition for Reconsideration and Request for Stay on January 15, 2002, and pursuant to an Order issued by the Commission on January 23, 2002, the unredacted version was made available on February 6, 2002. Thus, contrary to Verizon's assertion at Verizon's October 27, 2003 *ex parte* at 3 n. 1, Verizon, by redacting the data and then repeatedly opposing disclosure, successfully delayed the release of the audit data for almost eight months; by that time the data, the latest of which was collected in September 2000, was almost

second Section 272 audit, Verizon will be able to delay the release of that audit data for an equivalent period of time. Moreover, as shown in AT&T's October 1, 2003 *ex parte*, there was no effective remedy for the Section 272 violations identified in the first Section 272 audit. Specifically: (1) the statute of limitations had run for a key violation, so that all the Commission could do was "admonish" Verizon; and (2) Verizon deviated from the auditing guidelines, providing data in a format that precluded the Commission from determining whether other violations occurred.[7]

***Third, GNI's now conceded joint use of the LEC's OSS will "inevitably" lead to discrimination and cost misallocation.*** Verizon's October 27, 2003 *ex parte* makes it clear that if the OI&M forbearance petition is granted, Verizon will be using "the local exchange carrier's OSSs to provide OI&M services to the section 272 affiliate."[8] As the Commission found in the *Non-Accounting Safeguards Order*, allowing a BOC to provide network related services on behalf of an affiliate, "would *inevitably* afford the affiliate access to the BOC's facilities that is superior to that granted to the affiliate's competitors," and "would create substantial opportunities for improper cost allocation."[9]

This is made evident by Verizon's failure to address the inevitable risk that the LEC will provide its affiliate with *superior* access to its OSS.[10] Verizon also fails to explain its past claims that its LEC *cannot* provide unaffiliated IXCs with comparable direct access to their OSSs.[11] Nor has Verizon addressed the issue of likely cost misallocation with respect to the common OSS upgrades, as more fully explained in Dr. Selwyn's prior declaration in this proceeding -- that to the extent the OSS upgrade will be utilized on an integrated basis, the BOC could treat both the upgrade and subsequent ongoing maintenance expenses as a "common cost," and "*any non-zero allocation of these incremental system development and maintenance costs to POTS would have the effect of shifting costs away from the competitive long distance company and onto regulated monopoly local exchange service*" (emphasis in the original).[12]

***Fourth, Verizon utterly mischaracterizes its prior "absorption" claim in an attempt to minimize it.*** Verizon seeks to minimize the OI&M costs the LEC will "absorb," noting that in its June 24, 2003 *ex parte* it had stated that forbearance would only relieve it of *30%* of its "Workforce & Employee related expenses."[13] However, in that same *ex parte,* Verizon also stated that GNI would save *95%* of its costs for "Professional

---

18 months old. Verizon appears to be doing precisely the same thing with the second Section 272 audit data.

7 AT&T's October 1, 2003 *ex parte* at 6, n. 28.

8 *Id* at 4.

9 *Non-Accounting Safeguards Order* ¶ 12 (citing *BOC Separations Order*, 95 F.C.C.2d 1117 (1983)) (emphasis added).

10 Verizon states only that "the 272 affiliates and other carriers would only have access to data about their own networks in those OSSs" Verizon's October 27, 2003 *ex parte* at 3.

11 *See* AT&T's October 1, 2003 *ex parte* at 8 and note 36.

12 Ex Parte Declaration of Lee L. Selwyn, in CC Docket No. 96-149, July 9, 2003 ¶ 18.

13 Verizon's October 27, 2003 *ex parte* at 4.

Services," and *80%* of its "Back Office" expenses.[14] As previously shown by AT&T, not only are Verizon's savings claims utterly unsubstantiated,[15] but the magnitude of savings Verizon attributes to "absorption" by the LEC's workforce (whether 20%,[16] 30% or 80-95%) cannot be attributed to "efficiencies," as claimed by Verizon. At Verizon LD's level of operations, its network provider, GNI, should be operating at or near minimum average cost, *i.e.,* should have been able to achieve most or all of the potential economies of scale or scope (*i.e.*, should have achieved "minimum efficient scale"), such that the magnitude of any *bona fide* additional economies of scale would be minimal, perhaps even zero.[17] Thus, any savings above this level will result only because the LEC has excess capacity paid for by its ratepayers – excess capacity that it is now willing to provide to GNI for free.[18]

***Finally, Verizon doesn't contest AT&T's showing that even if CALLS were pure price caps Verizon would still have a powerful incentive to shift costs out of its long distance affiliates to enhance their ability to compete with nonintegrated rivals. In any event, Verizon has utterly failed to refute AT&T's showing that CALLS are not pure price caps.*** In its prior filings, AT&T demonstrated that even if CALLS were pure price caps, Verizon has strong incentives to discriminate against nonintegrated rivals and to misallocate costs.[19] Verizon's October 27, 2003 *ex parte* does not address that issue at all. Instead, Verizon cites to data on the number of retail lines Verizon lost in the last three years and the percentage of minutes of use on retail services lost in the last quarter,[20] challenging only AT&T's assertion about the likelihood that the Commission will reexamine ILEC price caps in July 2005 when *CALLS* expires. However, the data, even if correct, neither demonstrate that the level of competition is (or in 2005 will be) sufficient

---

14 *See* Verizon's June 24, 2003 *ex parte* at 7 (emphasis added) and Table 1 at 8-9.

15 Verizon failed to provide both affidavits by the persons Verizon identified as having "personal knowledge" explaining how these *ipse dixit* numbers were derived and the underlying data even though a Protective Order was in place. AT&T's October 1, 2003 *ex parte* at 3.

16 Verizon's October 30 letter to Commissioner Adelstein now suggests that the savings realized by having these services absorbed by the LEC will exceed 20% of its total savings. Letter from Kathryn C. Brown, Senior Vice President, Verizon, to Commissioner Jonathan S. Adelstein, October 31, 2003 at 2 ($39 million out of $183 million). AT&T would further note that the disclosure of the dollar figure in the Adelstein letter demonstrates the sham nature of Verizon's request for confidential treatment since this information was previously redacted.

17 AT&T's October 1, 2003 ex parte at 4-5.

18 AT&T further demonstrated that Verizon could achieve the same savings by having third party call center operators provide these services, thereby retaining the benefits of structural savings and allowing Verizon to avoid the construction and operation costs it claims it has incurred by providing OI&M services. *Id.* at 5.

19 *See e.g.*, Ex Parte Declaration of Lee L. Selwyn, appended to AT&T's Comments CC Docket No. 96-149 (November 15, 2002) ¶¶ 44-45; Declaration of Lee L. Selwyn appended to AT&T's Comments in the *Non-Dominance FNPRM* (June 30, 2003) ¶¶ 97-103; Reply Declaration of Lee L. Selwyn appended to AT&T's Comments in the *Non-Dominance FNPRM* (July 28, 2003) ¶¶ 57-58.

20 Verizon's October 27, 2003 *ex parte* at 4.

to constrain rates effectively[21] nor change Verizon's current incentives to misallocate costs regardless of whether or not the Commission ultimately reexamines ILEC price caps in July 2005.

Sincerely,

Aryeh Friedman

cc: B. Tramont
C. Libertelli
M. Brill
J. Rosenworcel
D. Gonzalez
L. Zaina
W. Maher

[21] *See, e.g.*, AT&T's Comments, WC Docket No. 02-112 and CC Docket No. 00-175, June 30, 2003 at 17, and because